CHESTERFIELD COUNTY

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LANE B. RAMSEY
COUNTY ADMINISTRATOR

October 11, 2002

The Honorable Members of the Board of Supervisors
County of Chesterfield, Virginia

Members of the Board:

We are pleased to submit to you the Comprehensive Annual Financial Report (CAFR) of Chesterfield County (the 'County') for the fiscal year ended June 30, 2002. State law requires that all local governments have all their accounts and records, including all accounts and records of their constitutional officers, audited annually as of June 30 by an independent certified public accountant and that an audited financial report is submitted on or before November 30 to the Auditor of Public Accounts of the Commonwealth of Virginia (APA). This report has been prepared by the Accounting Department in accordance with the standards of financial reporting as prescribed by the Governmental Accounting Standards Board (GASB), the Financial Accounting Standards Board (FASB), and the APA.

The CAFR was prepared with an emphasis on full disclosure of the financial activities of the County. Responsibility for both the completeness and the reliability of the contents rests with County management. To provide a reasonable basis for making these representations, management of the County has established a comprehensive internal control framework that is designated both to protect the government's assets from loss, theft, or misuse and to compile sufficient reliable information for the preparation of the County's financial statements in conformity with accounting principles generally accepted in the United States of America (GAAP). Because the cost of internal controls should not outweigh their benefits, the County's comprehensive framework of internal controls has been designed to provide reasonable rather than absolute assurance that the financial statements will be free from material misstatement. As management, we assert that, to the best of our knowledge and belief, this financial report is complete and reliable in all material respects.

KPMG LLP, a firm of licensed certified public accountants, audited the County's financial statements. The goal of the independent audit was to provide reasonable assurance that the basic financial statements of the County for the fiscal year ended June 30, 2002, are free of material misstatement. The independent audit involved examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements, assessing the accounting principles used and significant estimates made by management, and evaluating the overall financial statement presentation. The independent auditor concluded, based upon the audit, that there was a reasonable basis for rendering an unqualified opinion that the County's financial statements for the fiscal year ended June 30, 2002, are fairly presented in conformity with GAAP. The independent auditors' report is presented as the first component of the financial section of this report.

The independent audit of the financial statements of the County was part of a broader, federally mandated "Single Audit" designed to meet the special needs of federal grantor agencies. The standards governing Single Audit engagements require the independent auditor to report not only on the fair presentation of the financial statements, but also on the audited government's internal controls and compliance with legal requirements, with special emphasis on internal controls and legal requirements involving the administration of federal awards. These reports are available in the compliance sections of this report.

GAAP requires that management provide a narrative introduction, overview, and analysis to accompany the basic financial statements in the form of Management's Discussion and Analysis (MD&A). This letter of transmittal is designed to complement MD&A and should be read in conjunction with it. The County's MD&A can be found immediately following the report of the independent auditors.

Profile of the Government

The County is located in east-central Virginia, adjacent to the City of Richmond, and is a growing suburban, residential area, with concurrent commercial growth and industrial development. The County encompasses a land area of approximately 446 square miles with a population of approximately 264,000. A large portion of the land in the County, especially in the southwestern area, remains rural. The County is empowered to levy a property tax on both real and personal properties located within its boundaries.

Effective January 1, 1988, the County began operating pursuant to a County Charter approved by the citizens of the County in a referendum election and subsequently enacted by the Virginia General Assembly. The County is an independent political subdivision of the Commonwealth of Virginia with no subordinate political entities within its borders and the County is absolutely immune from annexation by adjacent localities. The governing body of the County is the Board of Supervisors (the "Board") that establishes policies for the administration of the County. The Board is composed of five members, one member elected from each of five magisterial districts. A member must be a resident of the district that he serves. Members are elected for four-year terms. A new Board was elected on November 2, 1999. The Board appoints a chief executive officer known as a County Administrator, who serves at the pleasure of the Board and carries out the policies established by the Board.

The County provides a full range of municipal services. Major programs include public safety, health and welfare, parks, recreation and cultural activities and community development. Additionally, the County operates an airport and water and wastewater utility systems.

The financial reporting entity includes all of the funds of the County, the primary government, as well as all of its component units. Two discretely presented component units, the School Board and the Health Center Commission, are included in the reporting entity because of the County's financial accountability for these organizations; however, these component units are reported in separate columns in the County's basic financial statements. Additional information on these legally separate organizations can be found in Note 1 in the notes to the financial statements.

The annual budget serves as the foundation for the County's financial planning and control. In November, County departments receive an expenditure target. Departments submit budgets and work plans, base on this target, to the County Administrator for review in January. Requests for additional funding by departments are negotiated and the County Administrator's proposed budget is prepared and submitted to the Board prior to March 15. The County is required to hold a public hearing on the proposed budget and to adopt a final budget by May 1. The appropriated budget is at the function level for the General Fund and at the fund level for the Comprehensive Services Fund. The County Administrator is authorized to amend appropriations by transferring unencumbered appropriated amounts within appropriation function or to increase any appropriation function up to $20,000. The Board must approve most other amendments that increase the total appropriation of any function level. Budgetary comparisons are provided in this report for each individual governmental fund for which an appropriated annual budget has been adopted. For the general fund, this comparison is presented on page 29 as part of the basic financial statements for the governmental funds. For governmental funds, other than the general fund, with appropriated annual budgets, this comparison is presented in the supplementa1 information section of this report, which starts on page 83. Also included in the supplemental information section is a project-length budget-to-actual comparison for each governmental fund for which a project-length budget has been adopted.

Factors Affecting Financial Condition

The information presented in the financial statements is perhaps best understood when it is considered from the broader perspective of the specific environment within which the County operates.

Local economy

The economic downturn and uncertainties on the local, state, and national levels during 2001 and early 2002 led the County to implement restraints in spending during fiscal year 2002 and budget reductions in fiscal year 2003. The County will also experience reductions in funding from the Commonwealth of Virginia due to its revenue shortfalls for fiscal years 2002-2004. The continued economic weakness into 2002 led economists to abandon expectations of a quick recovery from the recession that began in March 2001. A slow recovery is expected through 2003, with growth rates in revenue sources such as sales taxes, transient occupancy taxes, and personal property taxes rebounding to pre-recession levels by 2004. Despite the economic woes of 2001-2002, the real estate market remained strong in the County driven by low interest rates and land availability. The growth in real estate tax and recordation tax revenue associated with this strength may not continue in future years as interest rates increase.

The County's unemployment rate for 2001 averaged 2.5%, up from 1.5% the previous year. However, the County faired better than the 2001 unemployment rate of the Richmond-Petersburg area of 3.4% and the Commonwealth of Virginia of 3.5%.

Chesterfield recognizes the importance of expanding the business tax base to provide revenues for needed services and has made a commitment to promoting economic development. New economic activity for fiscal year 2002 included both commercial and industrial projects. The Department of Economic Development assisted with existing company expansions and new company locations. New and expanding businesses invested nearly $88.3 million and created approximately 500 new jobs. Taxable retail sales for calendar year 2001 increased by 1.4% to $2.6 billion.

Philip Morris USA invested $8 million to relocate its Information Technology Division from the City of Richmond to Chesterfield County. This division, which supports the company's manufacturing operations, moved 350 employees to the new 75,000 square foot site.

The most significant industry expansions in the County were Devon USA and Honeywell. Devon USA announced that it will start construction on an additional 506,000 square feet of warehouse and distribution space to be located in three new buildings. The three facilities, an investment of $11 million, will be complete by the end of 2003. The Specialty Materials business of Honeywell is expanding production of its Spectra high modulus polyethylene fiber product. The expansions will provide 6,300 additional square feet to support an emerging increase in the demand for Spectra products. Phase I, an investment of approximately $20 million, was completed at the end of September 2002.

Office buildings in the County account for the majority of space in the southwestern quadrant of the metropolitan Richmond area market. The quadrant's office vacancy rate increased from 11.5% as of June 2001 to 16.2% for June 2002. *Grubb & Ellis / Harrison & Bates* indicated that although demand for space is down, the supply is not extreme and Richmond's office market remains healthier than cities such as Atlanta and Raleigh.

The County is considered to have the best available location, the Meadowville Technology Park located off I-295, for the next semiconductor chip manufacturing company. In addition to this area, the creation of the Virginia Bio Technology Research Park at Meadowville will allow the County and the research park to jointly market prospects for either site and increase biotechnology sciences in the Richmond area. The Meadowville research park, a satellite location that is only 15 miles from the main Virginia Bio Technology Research Park in downtown Richmond, will have the capacity for approximately 2 million square feet of combined office, laboratory and manufacturing space. Also, the construction of the final leg of the Route 288 corridor through northwestern Chesterfield County to the west side is expected to become one of the region's premier office and light industrial employment centers.

A major regional project for area jurisdictions is the expansion of the Richmond Centre, which will increase this convention facility to almost three times its current size. On January 9, 1998, the County, in conjunction with three other participating jurisdictions (the Counties of Hanover and Henrico, and the City of Richmond) created the Greater Richmond Convention Center Authority (Convention Authority). The Convention Authority was created to acquire, finance, expand, renovate, construct, lease, operate, and maintain the facility and grounds of a visitors and convention center or centers including the current Richmond Centre facility. The primary purpose of the Convention Authority is to finance the expansion of the project and to operate and maintain the facility once construction is complete. The first phase of the expansion opened in the spring of 2001, which included the ballroom, parking deck, central plant, administrative offices, and meeting space. The second phase of the expansion is expected to be complete in January 2003.

Long-term financial planning

The County annually prepares a six-year Capital Improvement Program (CIP). The fiscal year 2003-2008 CIP serves as a planning tool for the efficient, effective, and equitable distribution of public improvements throughout the County. The CIP advances priorities established in recent years and lays the foundation for a future referendum now that the last increment of bonds authorized with the 1996 referendum were sold in FY2002. This CIP totals $568.6 million, and is comprised of County improvements of $193.0 million, School Board improvements of $264.7 million, and Utilities Department improvements of $110.9 million.

The County's most significant planned improvements include a new community development building, an expansion of the health and social services building, and a new local jail. The community development building is a new 80,000 – 100,000 square foot facility to consolidate community development departments from existing buildings. The estimated cost is $21.8 million and design is underway with expected completion in 2005. The first full year of operating costs are projected to be approximately $300,000 beginning in fiscal year 2007. The health and social services building expansion will add an additional 45,000 square feet. The addition is needed to alleviate a shortage of workspace for staff. The estimated cost is $12.4 million and planned for funding over the period of fiscal year 2005 – 2007. The County plans to replace its local jail facility. The existing facility has deteriorated and the replacement project contemplates demolition of the older buildings combined with reconstruction of new space. The estimated project cost is $24.8 million and should be fully funded by fiscal year 2004. No estimate of operating costs has been determined at this time.

Other major projects in the CIP include new fire stations, continued expansion of the police and fire training center, and an investment in emergency technology systems to compliment the recently completed enhanced emergency communications system. The CIP also proposes one new library, expansions and renovations to four existing libraries, new parks and recreation facilities, and reinvestments in existing parks and recreation facilities. The School Board major planned improvements includes new schools and improvements of $130.1 million, classroom additions of $20.5 million, and computer upgrades and replacements of $19.5 million.

The County is fortunate to have three different water resources, more than most localities enjoy. Two of these resources are reservoirs that have been particularly impacted by the drought during the fiscal year. In cooperation with our southern neighbors in the Appomattox River Water Authority (Water Authority), progress was made in securing an additional facility that will provide off-stream water storage pumped from the Appomattox River during periods of high flow. The water will be held in this storage facility until needed when the river is at low levels.

Cash management policies and practices

The County Treasurer follows a deposit and investment policy in accordance with the Commonwealth of Virginia statutes. The Treasurer determines cash flow needs and funds are invested daily in various maturities to meet cash flow requirements and maximize earnings. Temporary idle funds are automatically invested overnight in repurchase agreements that are secured or collateralized by governmental securities as required by the Code of Virginia. Deposits and investments during the year consisted of demand deposits, savings accounts, certificates of deposit, a money market fund, Virginia Local Government Investment Pool, repurchase agreements, stocks and bonds, direct obligations of the US Treasury, Virginia State Non-Arbitrage Program, and an open-ended mutual fund. The maturity of the investments range from one day for repurchase agreements to two years for obligations of the US Treasury, with an average maturity of 187 days. The average yield on investments in 2002 was 3.09%, which exceeded the three-month U.S. Treasury Bill average (2.17%) and the Donoghue's Money Fund average (2.12%) by 92 and 97 basis points, respectively. Investments with a maturity date of more than one year from date of purchase are stated at fair value and investments with a maturity date of one year or less from the date of purchase are stated at amortized cost. Decreases in fair value during the current year, however, do not necessarily represent trends that will continue; nor is it always possible to realize such amounts, especially in case of temporary changes in the fair value of investments that the government intends to hold to maturity.

Risk management

The Risk Management Department provides protection from losses of property, casualty, and liability claims for the County and the School Board. Third party coverage is obtained for real and personal property and certain liability risks. Third party property and casualty coverage is maintained for the Fire Department. The County maintains a broad form Public Officials Liability insurance policy to provide catastrophe coverage for individual claims in excess of $2.0 million. Risk Management revenues are generated by charges to the departments based on management's estimate of the cost of predicable losses, the cost for administering these losses, a pro rata share of insurance premiums paid, actuarial estimates for incurred but not reported claims and the Risk Management Department's operational costs.

Worker's compensation claims are funded annually by appropriation in the various funds. The County maintains an excess insurance policy for those claims greater than $250,000. Claims are administrated by the Risk Management Department.

Additional information on the County's risk management activity can be found in Note 11 of the notes to the financial statements.

Pension and other post employment benefits

The County contributes to the Virginia Retirement System (VRS), a mixed agent and cost-sharing multiple-employer defined benefit pension plan administered by the VRS, for all full-time employees. VRS uses an actuarial basis specified by the Code of Virginia and approved by the VRS Board of Trustees to determine the localities contributions to the plan. The County's actual contribution matched the annual required contribution for fiscal year 2002. The County currently has a net pension obligation due to its election to phase-in funding of the cost of living adjustment for 1998. The County, as of the actuarial valuation date of June 30, 2001, carried plan assets in excess of the actuarial accrued liability by 5.21%.

The County sponsors a single-employer defined benefit pension plan that covers certain qualified County employees in addition to any benefits that may be received under VRS and Social Security. The plan provides for annual employer contributions at actuarially determined rates which will remain relatively level over time as a percentage of payroll and will accumulate sufficient assets to meet the cost of all basic benefits when due. The County's actual contribution for 2002 matched the annual required contribution as determined in the July 1, 2001 actuarial valuation. The County currently has a net pension obligation and has funded 60.73% of the actuarial accrued liability determined as of July 1, 2002. The remaining unfunded actuarial accrued liability is being funded using a 40-year open amortization period.

The County provides postretirement health and dental care benefits for all full-time, salaried permanent employees who retire at or after age 55 with at least five years of credited service. As of the end of the current fiscal year, there were 491 retired employees receiving these benefits, which are financed on a pay-as-you-go basis. GAAP do not require governments to report a liability in the financial statements in connection with an employer's obligation to provide these benefits.

The School Board also provides its employees with a pension plan through VRS, a supplemental retirement program plan, and postretirement health and dental care benefits.

Additional information on the County's and School Board's pension arrangements and postretirement benefits can be found in Notes 12 and 13 in the notes to the financial statements.

Awards and Acknowledgements

The Government Finance Officers Association of the United States and Canada (GFOA) awarded a Certificate of Achievement for Excellence in Financial Reporting to Chesterfield County for its Comprehensive Annual Financial Report (CAFR) for the fiscal year ended June 30, 2001. This was the twenty-first consecutive year that the County has achieved this prestigious award. In order to be awarded a Certificate of Achievement, a government must publish an easily readable and efficiently organized comprehensive annual financial report. This report must satisfy both accounting principles generally accepted in the United States of America and applicable legal requirements.

A Certificate of Achievement is valid for a period of one year only. We believe our current CAFR continues to meet the Certificate of Achievement Program's requirements and we are submitting it to GFOA to determine its eligibility for another certificate.

The Budget and Management Department received an award for Distinguished Budget Presentation from GFOA, making Chesterfield one of only a few local governments in the country to receive the award for eighteen consecutive years. By earning this award, Chesterfield again demonstrates the strong leadership that is needed to handle the challenges that face local governments on a daily basis.

The National Institute of Governmental Purchasing (NIGP) of the United States, Canada, Ireland, and England established a new agency accreditation program which recognizes excellence in public purchasing by establishing a body of standards that should be in place for a quality purchasing operation. On October 25, 1999, the NIGP awarded the Chesterfield County Purchasing Department the Outstanding Agency Accreditation Achievement Award for demonstrating excellence in public purchasing. Chesterfield County's Purchasing Department was the eighth agency overall and the first locality or state agency in Virginia to receive this award.

We would like to express our appreciation to the staff of the Accounting Department who contributed to the timely preparation of this report. We would also like to thank the members of the Board of Supervisors for your interest and support in planning and conducting the financial operations of the County in a responsible and progressive manner.

Respectfully submitted,

Lane B. Ramsey

Lane B. Ramsey
County Administrator

Mary Lou Lyle

Mary Lou Lyle
Director of Accounting